

PYRAMID ENERGY INC.

1998 ANNUAL REPORT

AR60





CORPORATE PROFILE

Pyramid Energy Inc. is a junior oil and gas company based in Calgary, Alberta and publicly trades on The Alberta Stock Exchange under the symbol "PYI".

Pyramid Energy was started as a Junior Capital Pool company in December, 1996. In October, 1997 it acquired Pyramid Resources Ltd. as its Major Transaction. It also acquired Canadian Delta Exploration Ltd., a Private Corporation, as of January 1, 1998. Through vertical amalgamation, Pyramid Energy Inc. became the sole surviving entity effective January 1, 1999.

The Company owns and operates oil and gas properties in both Alberta and Saskatchewan. Participating in a Joint Venture with Pakistan Petroleum Limited in the Mid Indus Basin of South Central Pakistan, the Company made a significant gas discovery in March, 1998.

Pyramid's corporate strategy is to continue developing international oil and gas opportunities while maintaining and growing its Canadian asset base through corporate mergers and acquisitions, and drilling low risk exploration and development prospects. The Company is technically and financially strong and is committed to maintaining low general, administrative and overhead costs. Pyramid's Board members are seasoned industry professionals with strong connections both in Canada and overseas.

ANNUAL GENERAL MEETING

The Annual Shareholder's Meeting of the Company will be held on Friday, May 14, 1999 at 10:00 a.m. in the +15 Meeting Room, Altius Centre, 500 - 4th Avenue S.W., Calgary, Alberta.

ABBREVIATIONS

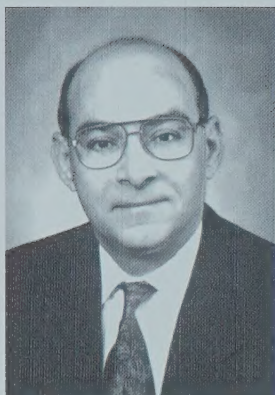
mcf	thousands of cubic feet
mbbls	thousands of barrels
mmcf	millions of cubic feet
bbl	barrel
Bcf	billions of cubic feet
NGL	natural gas liquids
boe	barrels of oil equivalent (10 mcf = 1 bbl)

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Year ended December 31,	1998	1997	% Change
FINANCIAL			
(\$, except where noted)			
Petroleum and natural gas sales (net)	2,543,272	1,704,460	+49
Cash flow from operations	1,153,943	831,768	+39
-per share, average outstanding	0.04	0.06	-33
Net capital expenditures	5,475,967	2,815,519	+94
Total assets	10,387,442	10,086,639	+3
Shareholders' equity	8,182,869	8,906,142	-8
Common shares outstanding			
-average for year (thousands)	26,967	13,534	+99
-at year end (thousands)	26,967	24,371	+11
OPERATIONS			
Crude oil and NGL production			
Barrels	86,115	49,725	+73
Barrels per day	236	136	+73
Average selling price (\$/bbl)	15.72	23.82	-34
Natural gas production			
Thousands of cubic feet	672,554	333,797	+101
Thousands of cubic feet per day	1,843	915	+101
Average selling price (\$/mcf)	2.05	2.28	-10
Average production (boe per day)	420	228	+84
Average selling price (\$/boe)	17.83	23.54	-24
Reserves (Proved plus Probable)			
Crude oil and NGL (thousands of barrels)	880	553	+59
Natural gas (millions of cubic feet)	7,907	6,116	+29
Wells drilled			
Gross	16	7	+129
Net	5.98	2.04	+193
Undeveloped land holdings (acres)			
Gross	754,958 ⁽¹⁾	866,549 ⁽¹⁾	-13
Net	114,505 ⁽¹⁾	133,100 ⁽¹⁾	-14

⁽¹⁾ Includes Pakistan land holdings.



A.D. (Tony) Anton
President

The year 1998 has been one of considerable uncertainty in the oil and gas sector. The oil price slide during 1997 continued into 1998 culminating in December with inflation adjusted prices reaching their lowest level in 25 years. The anticipated rise in gas prices did not fully materialize as winter weather in North America was much warmer than originally anticipated. These low commodity prices have resulted in lower than expected revenues and cash flows.

Through it all, Pyramid managed to stay the course with the following major achievements during the year:

- ▲ Closed the acquisition of Canadian Delta Exploration Ltd., adding approximately 85 boe per day to the Company's production;
- ▲ Drilled a major gas discovery in Pakistan;
- ▲ Added significantly to Pyramid's gas production with the drilling of two gas wells in Medicine Hat, Alberta;
- ▲ Completed the vertical amalgamation of the Pyramid companies with Pyramid Energy Inc. being the sole surviving entity;
- ▲ Commenced a share buy-back program aimed at enhancing shareholder value; and
- ▲ Extended the expiry dates of the Company's outstanding warrants to October 31, 1999.

In Western Canada, Pyramid participated in the drilling of 16 gross wells with limited success. Several high risk, high reward exploration prospects were drilled but, unfortunately, were unsuccessful.

In Pakistan, the Hasan X-1 well, the second well in Block 22, is scheduled to spud at the end of February with results becoming available in early April. The well is expected to test the "D" structure with a reserve potential of some 100 Bcf.

During the course of 1998 several prospective corporate merger candidates were evaluated, and one was pursued almost fully, but without success. As well, a bid was made on a significant producing property made available by a major integrated company. Although Pyramid's bid was among those considered successful, the Vendor elected to accept another bid.

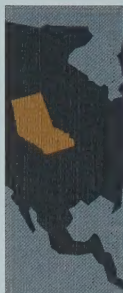
Through its share buy-back program which was first introduced on July 16, 1998, the Company acquired 1,097,591 shares at an average price of \$0.17/share. When compared with an asset value of \$0.37/share, the program has thus far achieved its objective.

Pyramid is approaching the new millennium with strong fundamentals - a solid production base, a healthy balance sheet and sufficient cash flow to carry out a modest-size development drilling program in 1999. Emphasis will again be placed on consummating a second corporate merger to further strengthen Pyramid's presence in Western Canada. Our search for an attractive international opportunity continues with the hope of securing same before year end.

A handwritten signature in black ink, appearing to read 'A.D. Anton', enclosed within a circular stamp or seal.

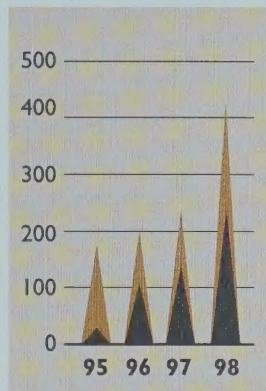
A.D. (Tony) Anton
President

Western Canada



During 1998, Pyramid's daily oil and NGL production averaged 236 barrels per day, an increase of 73 percent over 1997. Daily gas production for 1998 totaled 1,843 thousand cubic feet per day, more than double that of 1997. On a barrel of oil equivalent basis, Pyramid's 1998 total of 420 boe per day was an increase over 1997 of 84 percent.

Pyramid participated in the drilling of 16 gross wells (5.983 net) during 1998. Of this total, eight gross wells (3.500 net) were exploration wells and eight gross wells (2.483 net) were development wells. This drilling program resulted in four gross oil wells (0.383 net) and four gross gas wells (2.267 net) for an overall success ratio of 50 percent and 44 percent on a gross and net well basis respectively. Exploration areas included the Doe Creek area in NE B.C., the Worsley, Albright, Utikima, Nipisi and Meyer Lake areas in NW and N Central Alberta and the Willesden Green and Medicine Hat areas in S Central and SE Alberta.



Production History boe/day

Oil
Gas



Major Exploration Areas

MEYER LAKE PROSPECT (OIL)

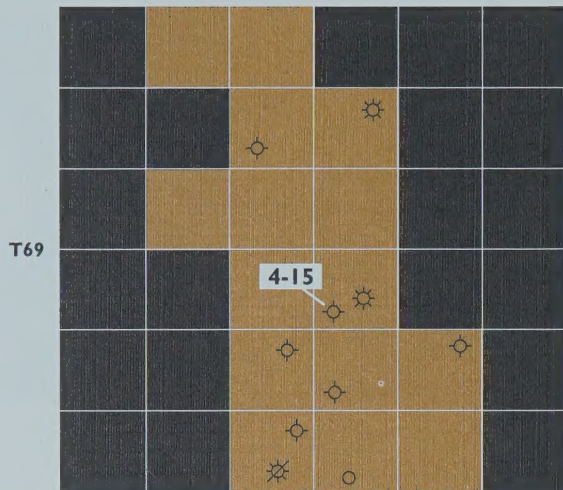
Pyramid farmed in on a 15 section land block in the Meyer Lake area by participating as to a 25 percent interest in the drilling of a Leduc test at 4-15-69-24 W4M. Although the well was abandoned, the potential for Leduc gas production exists in the area. Pyramid has the right to participate in a 25 township area and a possible participation right in an additional significantly larger area.

NIPISI PROSPECT (OIL)

Pyramid participated in re-entering a suspended Gilwood oil well located at 2-1-79-9 W5M, however, the Gilwood zone was found to be wet. A second undrilled prospect, identifiable by seismic, exists on one of the earned sections. Pyramid also has the right to participate as to a 25 percent interest in an additional ten-section option block.

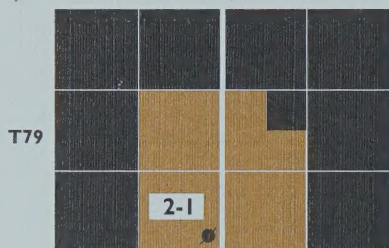
MITSTUE PROSPECT (OIL)

Pyramid farmed in on one and one-quarter sections of land in the Mitsue area. This land is adjacent to or in close proximity to several good oil wells producing from the Gilwood sand. One well was spudded at year-end at 11-25-73-5 W5M and is currently awaiting a stimulation program. A second well may be drilled in late 1999.

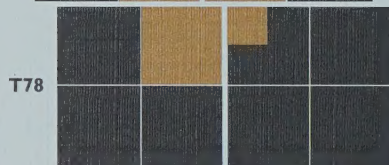


Meyer Lake

R24W4



T79



T78

R9W5

R8W5

Nipisi

- Pyramid Land
- Suspended Oil
- Abandoned Oil
- Dry Well
- Oil Well
- Oil and Gas
- Gas
- Suspended Gas
- Service
- Location



Mitsue

R5W5

R4W5

T74

T73

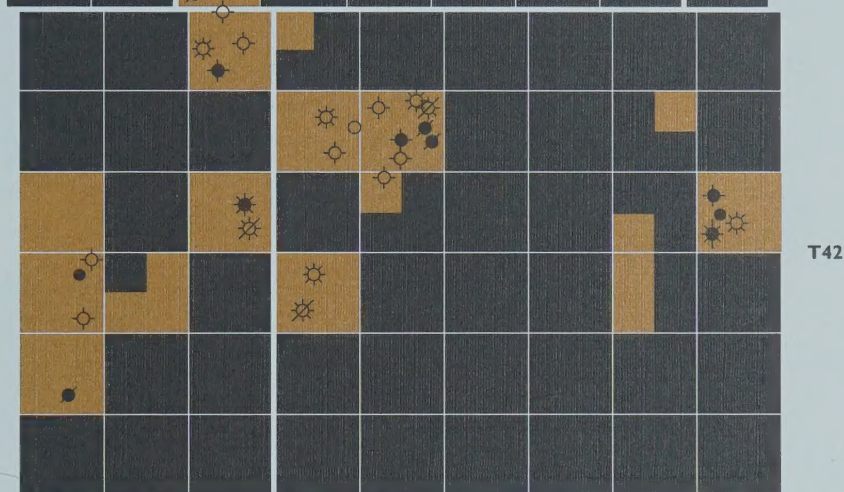
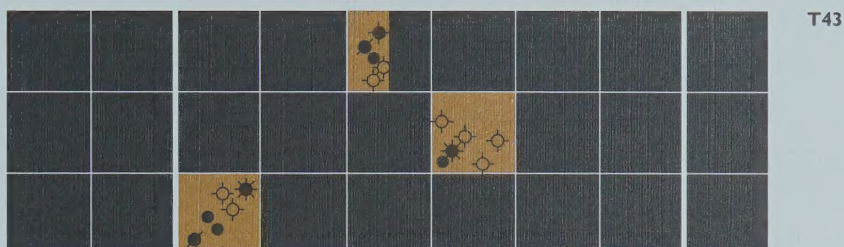
Major Production Areas

WOOD RIVER, CHIGWELL, BASHAW AREAS

The combined production of Pyramid's operated and non-operated properties in the general Wood River area accounted for approximately 150 boe per day or about 36 percent of the Company's daily production. Operated oil production was taken from three Leduc wells and one Ostracod well, while operated gas production was taken from two Belly River and three Basal Quartz wells. In addition to the Pyramid operated wells, there are two outside operated Belly River gas wells that produced gas throughout the year to the Apache Nevis Gas Plant. Pyramid's working interest in the general Wood River area averages about 50 percent except for a few properties.

MANIR CHARLIE LAKE UNIT

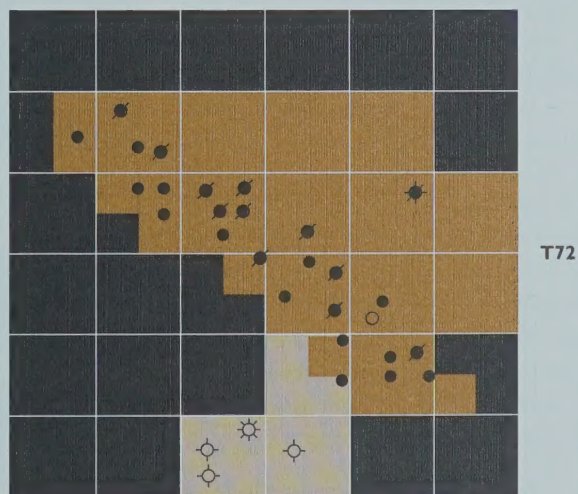
One new oil well was drilled in this unit near year-end. This unit, in which Pyramid has a 12 percent working interest, accounted for about 14 percent or 60 boe per day of Pyramid's daily average production. The operator is currently conducting water flood studies in an effort to increase oil recovery and production rates. The current re-injection of all the produced gas, to maintain reservoir pressure, has shown some success in maintaining oil production levels. The long-term plan for this unit is to allow some of the re-injected gas to be sold concurrently with the production of oil.



R24W4

R23W4

Wood River, Chigwell, Bashaw



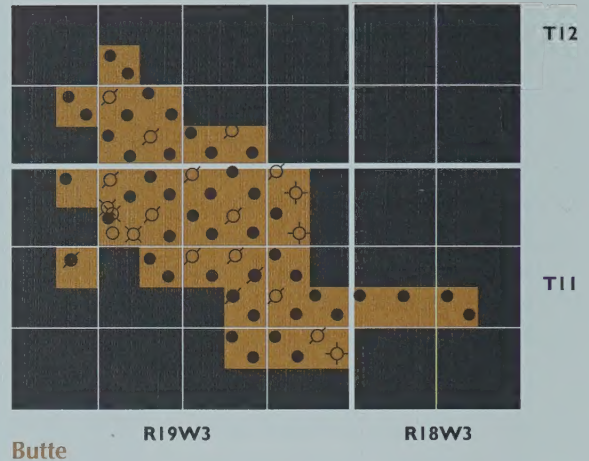
R3W6

Manir Charlie Lake

Pyramid Non-Unit Land

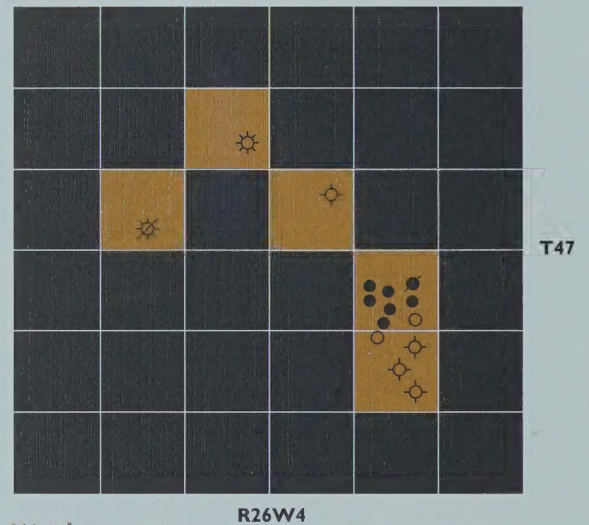
BUTTE VOLUNTARY UNIT

The Butte Voluntary Unit, Pyramid's only producing property in Saskatchewan, produced about 48 boe per day net to Pyramid during 1998. This production, which resulted from Pyramid's 6.50 percent interest in the unit, was about 12 percent of Pyramid's daily production. One new Upper Shaunavon oil well was drilled in the unit during 1998. This new well, combined with water flood operations and ongoing well maintenance, is forecast to hold production at the 1998 level during 1999.



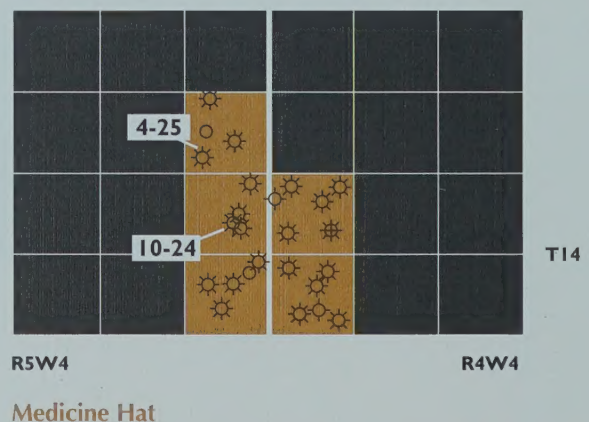
WATELET AREA

Pyramid's 10 percent interest in the Watelet Area contributed approximately 10 percent or 41 boe per day to the Company's 1998 daily production. Two new Ellerslie oil wells were drilled on the property during 1998. The operator may propose an additional well for 1999 pending the continued satisfactory performance of the current wells.



MEDICINE HAT AREA

Three wells were drilled by Pyramid during 1998 on three of the five sections of land that the Company holds in the Medicine Hat area. Pyramid's interest in these lands ranges from 75 percent to 100 percent. Two of these wells were successful and were producing about 1.8 mmcf per day at year-end from the Bow Island sand. A new location has been licensed and is scheduled to be drilled during the third quarter of 1999. Analysis of current gas production indicates that there may be the need to reduce the gas spacing unit in the field to one-half section from one section in order to adequately drain the gas reserves.

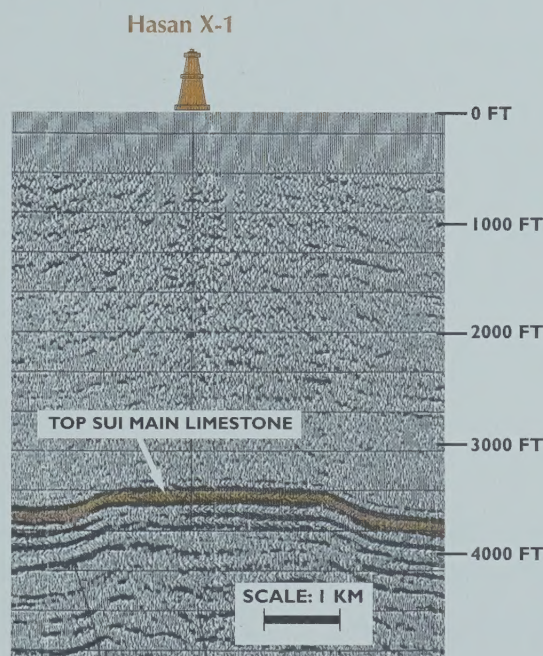


Review of International Operations - Pakistan



Early in 1998 Pyramid drilled two wells in Pakistan, one on each of its two large blocks of acreage in the Mid Indus Basin in South Central Pakistan. The Daud X-1 well on the Sadiqabad Block encountered good reservoir quality sand, however, the section contained no hydrocarbons due to absence of a reservoir seal. A geological assessment of the Block concluded that there was little prospect for discoveries and the Block will be surrendered. The Hamza X-1 well on Block 22 discovered gas in the Sui Main Limestone formation at approximately 1,200 meters and tested at a rate of approximately 8 mmcf/d.

As a result of the Hamza X-1 discovery a second well, Hasan X-1, is to spud in early 1999 to prove up additional reserves and deliverability prior to proceeding with full scale development and commencing production. The Hasan X-1 well is to be located on Prospect D (see seismic cross-section), the second of four recognized structures in Block 22. A reserve and economic evaluation of Block 22 by Chapman Petroleum Engineering Ltd., an independent consulting firm, determined Pyramid's share of unrisks probable plus possible reserves on Block 22 to be 26.5 Bcf with an undiscounted value of \$35 million. The following table summarizes the gas reserves and net present value determination:

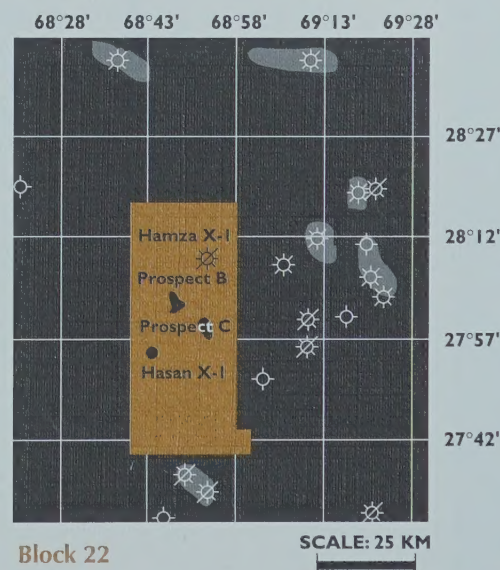


As at December 31, 1998	Gas Reserves (mmcf)	Cumulative Cash Flow, M\$ Cdn. ⁽¹⁾		
		Discounted at		
		0%	10%	15%
Probable	5,172	5,865	2,613	1,790
Possible	21,281	29,143	12,592	8,737
Probable plus Possible	26,453	35,008	15,205	10,527
Probable @ 50% plus				
Possible @ 25% ⁽²⁾⁽³⁾	7,906	10,218	4,455	3,079

(1) Before income tax

(2) The present worth of Pyramid's forecasted cash flows are net of \$4.388 million, un-escalated future capital expenditures.

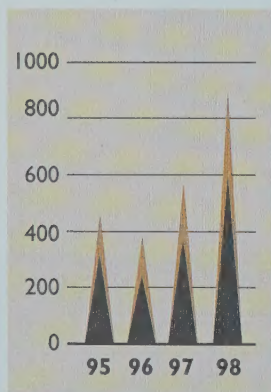
(3) The original evaluation was as of January 1, 1998, however, since the field is not producing, value as of December 31, 1998 is considered to be a close approximation.



Oil and Gas Reserves

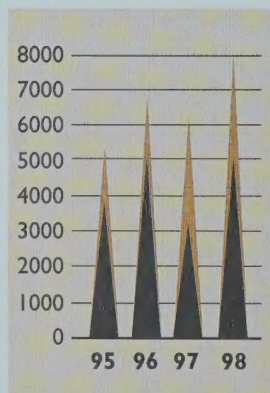
Pyramid's domestic oil and gas reserves are determined by Paddock Lindstrom & Associates Ltd., an independent petroleum consulting firm based in Calgary. Pyramid added 327 mbbls of oil and NGL to its proved and probable reserves as a result of the acquisition of Canadian Delta Exploration Ltd., effective January 1, 1998 and the continued development drilling at Watelet. Gas reserves increased by 1,791 mmcf mainly through exploration and development drilling at the newly discovered Medicine Hat field. The Manir Unit solution gas and gas cap reserves are booked as proved non-producing while undrilled acreage at Medicine Hat was allocated proved undeveloped and probable gas reserves.

Pyramid's oil and gas production was replaced 330 percent on a boe basis through reserve additions and acquisitions.



Reserves - Oil & NGL mbbls

■ Proved
■ Probable



Sales - Gas mmcf

■ Proved
■ Probable

Oil and Natural Gas Reserves⁽¹⁾

As at Year End	1998	1997
Oil and NGL, Proved Producing (mbbls)	566	318
Oil and NGL, Proved Non-Producing (mbbls)	11	42
Total Proved (mbbls)	577	360
Probable additional (mbbls)	303	193
Total Proved plus Probable (mbbls)	880	553
Sales Gas, Proved Producing (mmcf)	2,210	1,548
Sales Gas, Proved Non-Producing (mmcf)	1,878	1,630
Sales Gas, Proved Undeveloped (mmcf)	1,028	0
Total Proved (mmcf)	5,116	3,178
Probable additional (mmcf)	2,791	2,938
Total Proved plus Probable (mmcf)	7,907	6,116

⁽¹⁾ Probable reserves, unrisks

Reserve Life Index (in years)

	Proved	Proved + Probable
Oil and NGL	6.7	10.2
Sales Gas	7.6	11.8

The following discussion of Pyramid Energy Inc.'s operations is for the 1998 calendar year and reflects a full year of operations since the acquisition of Canadian Delta Exploration Ltd. Historical data, prior to becoming a publicly traded company in 1997, use audited financial statements and independent engineering evaluations of Pyramid Resources Ltd. which was later acquired by Pyramid Energy Inc.

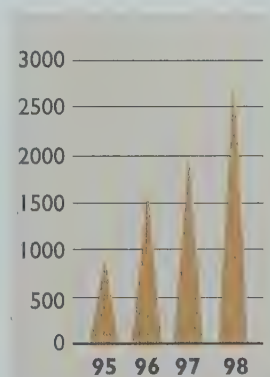
Net Present Value of Oil and Gas Reserves As at December 31, 1998	Discounted		
	0%	10%	15%
	\$000	\$000	\$000
Proved Producing	7,505	5,007	4,344
Proved Non-Producing	3,611	1,744	1,319
Proved Undeveloped	478	316	256
Total Proved	11,594	7,067	5,919
Probable additional ⁽¹⁾	3,158	1,347	1,007
Total Proved plus Probable	14,752	8,414	6,926
Alberta Royalty Tax Credit	1,101	903	830
Total Present Worth Value ⁽²⁾	15,853	9,317	7,756

⁽¹⁾ The Paddock Lindstrom evaluation values probable reserves at 50 percent of the per unit value assigned to proved reserves to allow for timing as well as geological and engineering risk associated with estimating probable reserves.

⁽²⁾ The present worth of Pyramid's forecasted cash flows are net of \$1.677 million of future capital expenditures.

REVENUE

Gross revenue, including interest income, increased 42 percent to \$2.83 million from \$1.99 million as a result of higher sales volumes from the acquisition of Canadian Delta and the development of the Medicine Hat gas project. Crude oil and natural gas liquids sales were 86,115 bbls, up 73 percent from 1997 sales of 49,725 bbls. The increase in crude production was from the Canadian Delta properties and continued development of the Watelet field. Gas sales totaled 673 mmcf, an increase of 101 percent from 1997 sales of 334 mmcf. The majority of this increase is from the Medicine Hat gas field developed during the year. The 1998 exit production was 450 boe per day.



Gross Revenue \$000

OPERATING COSTS

Operating costs totaled \$931,178, a 62 percent increase over the previous year. Again, the increase is attributable to the Canadian Delta acquisition and the Medicine Hat project. On a boe basis, operating costs actually decreased by 12 percent from \$6.90 per boe to \$6.07 per boe.

ADMINISTRATION COSTS

Administration costs for 1998 were \$526,551, an increase of 136 percent over 1997. Again, this increase is the result of the expanded operations of Pyramid. Significant consulting charges were incurred in association with large capital expenditures in 1998 and the heavy accounting load of managing three separate corporations. On a boe basis, administration costs increased by 28 percent from \$2.68 per boe to \$3.43 per boe.

Net Asset Calculation (in thousands except per share values)	1998	1997
Domestic Oil and Gas Reserves (<i>Proved plus Probable Discounted at 15% net present worth before tax</i> ⁽¹⁾⁽²⁾)	\$ 7,756	\$ 6,644
International Oil and Gas Reserves (Probable plus Possible Discounted at 15% net present worth before tax ⁽³⁾)	3,079	-
Undeveloped land and seismic	267	1,200 ⁽⁴⁾
Working Capital	(1,153)	3,552
Total	9,949	\$ 11,396
Common shares outstanding	26,967	24,371
Net asset value per share	\$ 0.37	\$ 0.47

⁽¹⁾ Probable reserves valued at 50% of their present worth value
⁽²⁾ Values include ARTC
⁽³⁾ Probable and possible reserves valued at 50% and 25% of their respective present worth values
⁽⁴⁾ Value includes Pakistan joint venture land valued at capitalized and equalization costs

INTEREST AND BANK CHARGES

With Pyramid's strong cash position during the year, interest and bank charges were minimal at \$33,611. These charges were more than offset by interest earned and other income of \$102,011. Interest and bank charges are expected to increase in 1999 as a result of drawing down the line of credit to fund the exploration and development program.

DEPLETION AND DEPRECIATION

Depletion and depreciation increased dramatically to \$3,445,909 from \$631,753 due to the higher production volumes and a one-time ceiling test writedown of \$2,300,000. The value for the year, excluding the writedown, was \$7.47 per boe, down \$0.13 from \$7.60 per boe in 1997.

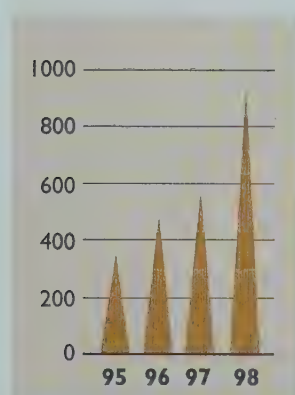
CAPITAL EXPENDITURES

Total funds spent by Pyramid during 1998 for drilling, completing and/or abandoning wells totaled \$4.92 million. Of this total \$1.66 million was spent to fund Pyramid's 15 percent share of two wells in Pakistan. An additional \$0.55 million was spent on land acquisitions, equipping wells, flowlines and seismic activities.

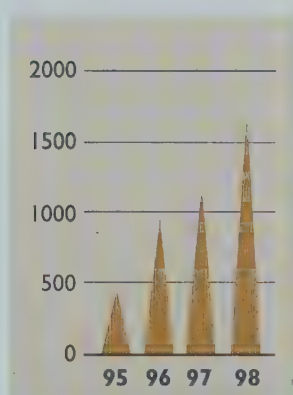
INCOME TAXES

Pyramid has available tax deductions for future years of \$7,976,513 at rates varying from 100 percent to 10 percent up from \$5,627,000 the previous year. A portion of 1998 exploration and development expenditures was funded through a 1997 issue of flow through shares. All of the qualifying flow through share expenditures of \$2,576,452 were expended in 1998.

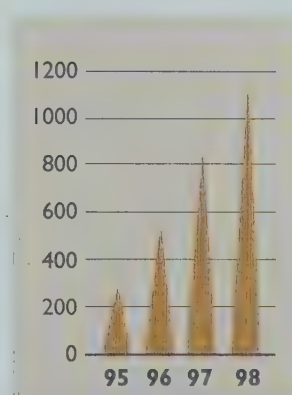
Tax Pool Summary		
<i>As at December 31, 1998</i>		
	Deduction Rate, %	Amount, \$
Canadian Exploration Expenses	100	248,744
Canadian Development Expenses	30	708,257
Canadian Oil and Gas Property Expenses	10	3,335,731
International Exploration Expenses	10	2,239,864
Undepreciated Capital Cost	20 - 30	1,177,195
Share Issue Costs	20	266,722



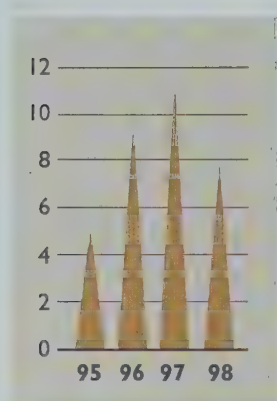
Operating Costs \$000



Net Operating Income \$000



Cash Flow \$000



Netbacks \$/boe

NETBACKS

Netbacks are calculated by charging royalties, operating and administrative costs against total revenue earned by each equivalent barrel of oil and gas produced. For comparative purposes, each 10 mcf of natural gas is converted to an equivalent barrel of oil which represents a general relative equivalent price relationship between the two commodities. Pyramid's netback per equivalent barrel in 1998 was \$7.76 compared to \$11.37 per equivalent barrel in 1997. This reduction is the result of the continued depressed crude price during the year.

CASH FLOW

Cash Flow (per barrel of oil equivalent @ 10 mcf = 1 barrel of oil)	1998	1997
Total Oil and Gas Sales	\$ 17.83	\$ 23.54
Royalties (net of ARTC) ⁽¹⁾	(1.24)	(3.03)
Operating Costs	(6.07)	(6.90)
Net Operating Income	\$ 10.52	\$ 13.61
Interest and Other Income	\$ 0.67	\$ 0.44
Administration Costs	(3.43)	(2.68)
Netback	\$ 7.76	\$ 11.37
Interest Expenses	(0.22)	(1.35)
Cash Flow	\$ 7.54	\$ 10.02

⁽¹⁾ Unclaimed 1997 ARTC credited to 1998

SHARE TRADING HISTORY

Pyramid's shares commenced public trading on the Alberta Stock Exchange on April 25, 1997 under the symbol "PYI". The price range and volume history for 1998 is shown in the following table:

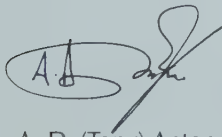
1998	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Year
Share price - \$					
High	0.73	0.66	0.44	0.40	0.73
Low	0.50	0.33	0.35	0.11	0.11
Weighted Average	0.66	0.51	0.39	0.15	0.37
Volume of shares traded	878,241	547,112	234,000	1,570,546	3,229,899

The accompanying consolidated financial statements were prepared by management in accordance with accounting principles generally accepted in Canada using estimates and careful judgement where necessary. Financial information presented throughout the Annual Report is consistent with that shown in the financial statements.

Management is responsible for the integrity of the financial statements. Systems of internal control are designed and maintained by management to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for financial purposes.

The external auditors conducted an independent examination of corporate and accounting records. Their examination included a review and evaluation of Pyramid's system of internal control and included such tests and procedures as they considered necessary to provide reasonable assurance that the financial statements are presented fairly.

The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and internal control. The Board of Directors, including members of the Audit Committee, meets with management and the external auditors to confirm that management's responsibilities are properly discharged and to review financial statements before they are approved.

A stylized handwritten signature in black ink, appearing to read 'A. D. Anton'.

A. D. (Tony) Anton
President

A handwritten signature in black ink, appearing to read 'H. J. Berry'.

Holland J. Berry
Vice-President
and Secretary Treasurer

To the Shareholders of Pyramid Energy Inc.

We have audited the consolidated balance sheets of Pyramid Energy Inc. as at December 31, 1998 and 1997 and the consolidated statements of operations and deficit and changes in financial position for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1998 and 1997 and the results of its operations and financial position for the years then ended in accordance with generally accepted accounting principles.

Calgary, Alberta
February 12, 1999


Chartered Accountants

CONSOLIDATED BALANCE SHEETS

December 31	1998	1997
ASSETS		
<i>Current</i>		
Cash and short-term deposits	\$ 48,390	\$ 4,300,473
Funds held in trust	524,053	-
Accounts receivable	412,219	406,495
Prepaid expenses	33,313	25,734
	1,017,975	4,732,702
Investment	13,882	13,882
Property and equipment (Note 5)	9,355,585	5,340,055
	\$ 10,387,442	\$ 10,086,639
LIABILITIES		
<i>Current</i>		
Bank indebtedness (Note 6)	\$ 1,418,982	\$ -
Accounts payable	765,504	1,180,497
	2,184,486	1,180,497
Site restoration and abandonments	20,087	-
	2,204,573	1,180,497
SHAREHOLDERS' EQUITY		
Capital stock (Note 8)	10,212,402	8,687,411
(Deficit) retained earnings	(2,029,533)	218,731
	8,182,869	8,906,142
	\$ 10,387,442	\$ 10,086,639
<i>Uncertainty (Note 11)</i>		

On behalf of the Board


Director


Director

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

<i>Years Ended December 31</i>	1998	1997
REVENUE		
Oil and gas sales	\$ 2,733,880	\$ 1,956,416
Royalties, net	(190,608)	(251,956)
Net production revenue	2,543,272	1,704,460
Interest and other income	102,011	36,303
	2,645,283	1,740,763
EXPENSES		
Operating	931,178	573,688
General and administrative	526,551	222,875
Depletion and depreciation	3,445,909	631,753
Interest - current	33,611	7,444
- long-term	-	104,988
	4,937,249	1,540,748
(Loss) earnings before income taxes	(2,291,966)	200,015
Income taxes recovered - deferred	43,700	-
Net (loss) earnings	(2,248,266)	200,015
Retained earnings, beginning of year	218,733	18,716
(Deficit) retained earnings, end of year	\$ (2,029,533)	\$ 218,731
(LOSS) EARNINGS PER SHARE	\$ (0.08)	\$ 0.01

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

<i>Years Ended December 31</i>	1998	1997
CASH DERIVED FROM (APPLIED TO)		
Operating		
Net (loss) earnings	\$ (2,248,266)	\$ 200,015
Depletion and depreciation	3,445,909	631,753
Deferred tax recovery	(43,700)	-
Cash flow from operations	1,153,943	831,768
Change in non-cash working capital	(409,720)	891,716
	744,223	1,723,484
Investing		
Addition to property and equipment	(5,475,967)	(2,815,519)
Net assets acquired on purchase of subsidiary	(1,937,760)	(13,882)
	(7,413,727)	(2,829,401)
Financing		
Issue of shares on acquisition of subsidiary	1,840,625	298,153
Repurchase of common shares	(194,777)	-
Offering costs	(123,356)	-
Issue of shares for cash	-	6,806,107
Repayment of long-term debt	-	(1,700,000)
	1,522,492	5,404,260
NET (DECREASE) INCREASE IN CASH	(5,147,012)	4,298,343
Beginning of year	4,300,473	2,130
End of year	\$ (846,539)	\$ 4,300,473
Cash flow from operations per common share	\$ 0.04	\$ 0.06

See accompanying notes to the consolidated financial statements.

December 31, 1998

1. NATURE OF OPERATIONS

The Company is primarily engaged in the exploration for and production of petroleum and natural gas in Alberta and Pakistan.

2. PRINCIPLES OF CONSOLIDATION

These financial statements include the accounts of the Company and its wholly-owned subsidiaries, Pyramid Resources Ltd. and Canadian Delta Exploration Ltd.

3. BUSINESS COMBINATION

Effective January 1, 1998, pursuant to an Offer to Purchase, Pyramid Energy Inc. (Energy) acquired all the issued and outstanding common shares of Canadian Delta Exploration Ltd. (CDE). As consideration, Energy issued 3,681,250 common shares on the basis of one share for one CDE share so acquired for a total consideration of \$1,840,625.

The acquisition has been accounted for using the purchase method from the effective date of acquisition. Details of the acquisition at assigned values are as follows:

Working capital	\$ (97,135)
Petroleum and natural gas properties	1,992,260
Deferred income taxes	(43,700)
Site restoration and abandonment costs	(10,800)
Aggregate net purchase price	\$ 1,840,625

The results of operations of CDE are reflected in the consolidated statements from the date of acquisition, January 1, 1998, to December 31, 1998.

Effective September 15, 1997, pursuant to an Offer to Purchase, Energy acquired all the issued and outstanding common shares of Pyramid Resources Ltd. (Resources). As consideration, Energy issued 11,373,500 common shares on the basis of one share for one Resources' share so acquired. As a result, the former shareholders of Resources hold in excess of 50 percent of the voting shares of the combined entity.

The transaction is referred to as a reverse take-over and, for accounting purposes, Resources is deemed to have acquired Energy. The deemed acquisition of Energy is accounted for by the purchase method and the fair value of the net assets acquired are:

Working capital deficiency, excluding cash	\$ (9,939)
Cash	308,092
	\$ 298,153

In accordance with accounting for a reverse take-over, the accumulated retained earnings of Energy, as at the acquisition date, is eliminated on consolidation. The value relating to share capital represents the share capital of Resources together with the cost of the purchase as determined above. The number of shares issued and outstanding reflects the number of Energy shares issued and outstanding including the number of shares issued to effect the reverse take-over.

The results of operations of Energy are reflected in the consolidated statements from the date of acquisition, September 15, 1997, to December 31, 1997.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with generally accepted accounting principles and reflect the following policies:

Petroleum and natural gas properties

The Company follows the full cost method of accounting for its petroleum and natural gas operations. Under this method all costs of exploration for and development of petroleum and natural gas reserves are capitalized. Costs include lease acquisition costs, geological and geophysical expenses, overhead directly related to exploration and development activities and costs of drilling both productive and non-productive wells. Proceeds from the sale of properties are applied against capitalized costs, without any gain or loss being recognized, unless such sale would significantly alter the rate of depletion and depreciation.

Depletion of exploration and development costs and depreciation of production equipment is provided on the unit-of-production method based upon estimated proven petroleum and natural gas reserves.

The carrying value of the Company's petroleum and natural gas properties and production equipment, net of recorded deferred income taxes, is compared annually to an estimate of future net cash flow from the production of proven reserves using year end prices, less estimated future general and administrative expenses, financing costs and income taxes. Should this comparison indicate an excess carrying value, the excess will be charged against earnings as additional depletion and depreciation.

Joint operations

Substantially all of the Company's petroleum and natural gas activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

Flow-through common shares

The Company credits capital stock with the proceeds of flow-through share issues less the estimated tax benefits transferred to the shareholders.

Future site restoration and abandonment costs

Estimated costs of future site restoration and abandonments, net of recoveries, are provided for over the life of proved reserves on a unit-of-production basis. An annual provision is recorded as additional depletion and depreciation. The accumulated provision is reflected as a non-current liability and actual expenditures are charged against the accumulated provision when incurred.

Earnings and cash flow per share

Earnings and cash flow from operations per share are based upon the weighted average number of shares outstanding during the year (1998 - 26,967,024; 1997 - 13,533,880).

The exercise of options and warrants referred to in Note 6 is non-dilutive.

Earnings per share for 1997 is computed based upon the number of shares of Pyramid Energy Inc. issued on the acquisition of Pyramid Resources Ltd. as outlined in Note 3, for the period from January 1, 1997 to September 14, 1997, the date of acquisition, and the actual number of shares of Pyramid Energy Inc. issued and outstanding during the period from the date of acquisition to December 31, 1997.

Office equipment

Office equipment is recorded at cost and depreciated on a diminishing balance basis over the estimated useful life of those assets.

Use of estimates

The preparation of the financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are subject to measurement uncertainty. Actual results could differ from and affect the results reported in these financial statements.

Financial instruments

The Company has estimated the fair value of its financial instruments which include cash, accounts receivable, bank indebtedness and accounts payable. The Company has used valuation methodologies and market information available as at year end and has determined that the carrying amounts of such financial instruments approximate fair value in all cases.

5. PROPERTY AND EQUIPMENT

	1998	1997
Petroleum and natural gas properties	\$ 14,096,942	\$ 7,204,381
Tax benefits transferred to shareholders	(1,448,650)	(1,448,650)
	12,648,292	5,755,731
Accumulated depreciation	(4,732,757)	(1,380,152)
	7,915,535	4,375,579
Production equipment	2,013,677	1,287,570
Office equipment	69,524	48,237
Accumulated depreciation	(643,151)	(371,331)
	1,440,050	964,476
	\$ 9,355,585	\$ 5,340,055

The Company has financed a portion of its exploration and development activities through the issue of flow-through shares. As a result, petroleum and natural gas properties with a cost of \$3,914,528 (1997 - \$1,104,413) have no cost basis for income tax purposes and are carried net of the estimated tax benefits transferred to shareholders.

The ceiling test for the year ended December 31, 1998, was completed using year-end prices for the year of \$12.93 per Bbl of oil and \$2.42 per MCF of gas, resulting in a write down of \$2,300,000 which is included in depletion and depreciation.

6. BANK INDEBTEDNESS

During the year, the Company established a credit facility consisting of a revolving demand loan to a maximum of \$2,500,000 and a Swap Facility to a maximum of \$500,000 US until June 30, 1999. The loan bears interest at bank prime plus 1/4 percent. Security is provided by a \$10,000,000 demand debenture conveying a first floating charge over all assets.

7. PROVISION FOR FUTURE SITE RESTORATION

At December 31, 1998 the costs, net of expected recoveries, relating to future site restoration and abandonments are estimated to be \$68,975 (1997 - \$ Nil) of which \$20,086 (1997 - \$ Nil) has been provided for.

8. CAPITAL STOCK

Authorized:

Unlimited number of common shares

Unlimited number of non-voting First Preferred shares, issuable in series

Unlimited number of voting Second Preferred shares, issuable in series

a) Issued and outstanding:	1998		1997	
	Number of Shares	Stated Value	Number of Shares	Stated Value
Beginning of year	24,370,865	\$ 8,687,411	9,419,500	\$ 2,836,151
Issued pursuant to:				
Issued for cash	-	-	1,944,000	793,151
Exercise of options	-	-	10,000	2,500
Shares issued and outstanding prior to acquisition	24,370,865	8,687,411	11,373,500	3,631,802
Adjustment on business combination	-	-	(8,723,500)	-
	24,370,865	8,687,411	2,650,000	3,631,802
Shares issued to acquire subsidiary (Note 3)	3,681,250	1,840,624	11,373,500	298,153
Shares issued for cash	-	-	10,347,365	4,980,526
Repurchase of common shares	(1,097,591)	(194,777)	-	-
Exercise of options	12,500	2,500	-	-
	26,967,024	10,335,758	24,370,865	8,910,481
Less share issued costs	-	(123,356)	-	(223,070)
	26,967,024	\$ 10,212,402	24,370,865	\$ 8,687,411

For the year ended December 31, 1997, shares issued for cash include 4,014,450 (1996 - 500,000) flow-through shares issued at \$0.70 (1996 - \$0.50) per share for proceeds of \$2,810,115 (1996 - \$250,000). Share capital has increased by \$1,557,115 (1996 - \$138,500) being proceeds less the tax benefits of \$1,253,000 (1996 - \$111,500) renounced to the shareholders.

b) Stock options

Under a stock option plan, common shares of the Company are, from time-to-time, reserved for issuance to eligible participants. At December 31, 1998, options for 2,065,000 shares (1997 - 977,500) were outstanding with exercise prices ranging from \$0.20 per share to \$0.55 per share (weighted average price being \$0.45 per share) and expiration dates between April 21, 2000 and August 7, 2003.

c) Warrants

As at December 31, 1998, pursuant to the issue of warrants on October 14, 1997, the Company has 6,332,915 and 617,500 warrants outstanding exercisable at one common share for each warrant outstanding at a price of \$0.70 and \$0.5263, respectively, until October 31, 1999. In addition, the Company has 3,681,250 warrants outstanding, issued on the acquisition of Canadian Delta Exploration Ltd. exercisable at \$0.70 per share until January 15, 2000. Warrants issued as compensation to a company for assistance with certain share issues remain outstanding. These consist of 150,000 warrants exercisable for one common share at \$0.40 until April 25, 1999 and 316,646 warrants exercisable at \$0.55 until October 14, 1999.

9. INCOME TAXES

Provision for income taxes

The total provision for income taxes differs from the expected amount calculated by applying the combined basic Federal and Provincial tax rate of approximately 45 percent to earnings before income taxes. This difference results from the following items:

	1998	1997
Expected income tax expense (recovery)	\$ (1,008,500)	\$ 89,200
Increase (decrease) resulting from:		
Non-deductible Crown charges	116,500	137,325
Resource allowance	(111,000)	(113,700)
Share issue costs	(46,000)	(22,000)
Other credits and adjustments	(6,700)	(81,725)
Unrecorded tax benefit from write down of petroleum and natural gas properties	1,012,000	-
Recovery through utilization of prior year tax losses	-	(9,100)
	\$ (43,700)	\$ -

Available tax deductions

As at December 31, 1998, the Company had available the following amounts which may be deducted in determining taxable income of future years. The amounts are deductible at the annual rates indicated:

	Rate	1998	1997
Canadian exploration expense	100%	\$ 248,744	\$ 440,000
Canadian development expense	30%	708,257	580,000
Canadian oil and gas property expense	10%	3,335,731	2,743,000
Foreign exploration expense	10%	2,239,864	870,000
Undepreciated capital cost	20% to 30%	1,177,195	815,000
Share issue costs	20%	266,722	179,000

10. SEGMENTED INFORMATION

Identifiable assets by geographic segment are as follows:

	1998	1997
Canada	\$ 7,735,108	\$ 9,293,097
Pakistan	2,652,334	793,542
	\$ 10,387,442	\$ 10,086,639

All revenues and expenses are wholly attributable to Canadian operations for both 1998 and 1997.

11. UNCERTAINTY DUE TO THE YEAR 2000 ISSUE

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using Year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

12. SUBSEQUENT EVENT

Effective January 1, 1999, the Company and its subsidiaries, Pyramid Resources Ltd. and Canadian Delta Exploration Ltd. were amalgamated pursuant to the provisions of the Alberta Business Corporations Act.

FOUR-YEAR SUMMARY

	1998	1997	1996	1995
FINANCIALS				
(\$, except where noted)				
Petroleum and natural gas sales	2,733,880	1,956,416	1,623,989	888,290
Royalties (net of ARTC)	(190,608)	(251,956)	(250,636)	(101,256)
Interest and other income	102,011	36,303	450	43,222
Expenses				
Operating costs	931,178	573,688	459,840	345,344
Administration	526,551	222,875	211,716	127,636
Interest	33,611	112,432	144,489	84,697
Depletion and depreciation	3,445,909 ⁽²⁾	631,753	432,061	421,973
Cash flow from operations	1,153,943	831,768	557,758	272,579
Per common share	0.04	0.06	0.05	0.04
Net earnings (loss)	(2,291,966)	200,015	125,697	(149,394)
Per common share	(0.08)	0.01	0.01	(0.02)
Working capital (deficiency)	(1,152,629)	3,552,205	(1,554,422)	(918,773)
Total assets	10,387,442	10,086,639	4,879,655	4,234,411
Capital expenditures	5,475,967	2,815,519	996,050	2,975,381
Shares				
Outstanding at year end	26,967,024	24,370,865	9,419,500	7,337,000
Average for year	26,967,024	13,534,127	11,373,500 ⁽¹⁾	7,337,000
OPERATING				
Production				
Crude oil and liquids (bbls)	86,115	49,725	39,736	9,490
Natural gas (mcf)	672,554	333,797	333,559	529,250
Reserves (Proved and Probable)				
Crude oil and gas liquids (mbbls)	880	553	388	452
Natural gas (mmcf)	7,907	6,116	6,695	5,318
Average Price				
Oil (per bbl)	15.72	23.82	25.10	21.41
Gas (per mcf)	2.05	2.28	1.92	1.32
Undeveloped lands				
Gross acres	754,958	866,549	9,920	2,560
Net acres	114,505	133,100	3,254	1,280
Drilling statistics (net)				
Oil and gas wells	8 (2.65)	6 (1.90)	3 (1.05)	1 (0.12)
Dry and abandoned wells	8 (3.33)	1 (0.14)	2 (0.35)	- -
Service wells	- -	- -	- -	1 (0.50)
Total wells	16 (5.98)	7 (2.04)	5 (1.40)	2 (0.62)
Percentage success rate	50 (44)	86 (93)	60 (75)	100 (100)

⁽¹⁾ Represents the number of shares issued by Pyramid Energy Inc. to acquire all the issued and outstanding shares of Pyramid Resources Ltd. as required for "reverse takeover" accounting.

⁽²⁾ Includes a one-time ceiling test writedown of \$2,300,000.

BOARD OF DIRECTORS AND OFFICERS

A. D. (Tony) Anton
President and Director

Holland J. Berry
Vice President,
Secretary-Treasurer and Director

S. S. (Said) Arrata*
Director

D. A. (Don) Smith*
Director

J. D. (Jack) McCleary*
Director

Andy Janisch
Director

** Member of Audit Committee*

LEGAL COUNSEL AND CORPORATE SECRETARY

Greg Powers, Q.C.
Donahue Powers Wells

BANKER

Canadian Imperial Bank of Commerce
Calgary, Alberta

STOCK EXCHANGE LISTING

PYI on the Alberta Stock Exchange

AUDITORS

Grant Thornton
Calgary, Alberta

ENGINEERS -

OIL & GAS EVALUATIONS

Paddock Lindstrom & Associates Ltd.
Calgary, Alberta

REGISTRAR & TRANSFER AGENTS

Montreal Trust
Calgary, Alberta





PYRAMID ENERGY INC.

Suite 1600, 500 - 4th Avenue S.W.
Calgary, Alberta, Canada T2P 2V6

Phone: (403) 531-9027

Fax: (403) 531-9026

E-mail: pyram3@cadvision.com

Web Site: www.pyramidenergy.net